

**DECISION
OF THE
ASSESSMENT APPEALS COMMITTEE**

CASE NO. 2008-01

Bank X (Bank), filed an appeal with the Assessment Appeals Committee (Committee) of the Federal Deposit Insurance Corporation (FDIC) by letter dated January 24, 2008. The Bank is appealing a determination issued by the FDIC's Division of Insurance and Research (DIR) on January 3, 2008. DIR denied the Bank's request to upgrade its capital evaluation from "Adequately Capitalized" to "Well Capitalized" for the April 1 to June 30, 2007 assessment period. The requested upgrade would place the Bank in Risk Category I for the relevant assessment period, subject to an assessment rate of five to seven basis points. With DIR's denial, the Bank remained in Risk Category II, subject to an assessment rate of 10 basis points. The Bank's quarterly deposit insurance assessment was \$64,414, approximately \$28,000 higher than it would have been if the Bank had not fallen below the Well Capitalized threshold. This appeal followed.

At its meeting held on March 12, 2008, after carefully considering all of the written submissions and facts of this case, the Committee has determined that the Bank's appeal must be denied.

BACKGROUND

On November 30, 2007, the Bank requested review by DIR of its capital evaluation for the April 1, 2007 assessment period, as provided for under 12 C.F.R. § 327.4(c). The Bank asserted that its Total risk-based capital ratio fell below the regulatory Well Capitalized threshold (10 percent – see 12 C.F.R. § 327.9(b)(1)) as of June 30, 2007, the result of a mathematical error by the Bank in its quarterly capital calculation. The Bank discovered its error sometime in July of 2007, while preparing its June 30, 2007 Call Report. According to the Bank, additional capital was injected from the Bank's parent company to return the Bank to Well Capitalized status.

With its Request for Review, the Bank included an August 6, 2007 letter from the Office of the Comptroller of the Currency (OCC) - its primary federal regulator. The OCC letter indicates that the Bank returned to Well Capitalized status after its holding company twice infused additional capital, once on July 31, 2007, and again on August 2, 2007. OCC determined the Bank to be Well Capitalized as of the later date.

By letter dated January 3, 2008, DIR denied the Bank's request for review of its assessment rate. DIR addressed the FDIC's regulations, specifically 12 C.F.R. § 327.9(b), which governs assignments of capital evaluations. DIR determined that the Bank did not satisfy the capital ratio standard for a Well Capitalized institution as of June 30, 2007, that the capital evaluation assigned for the assessment period beginning April 1,

2007 was correct, and that denial of the Bank's request was "consistent with the treatment of similarly situated institutions."

By letter dated January 24, 2008, the Bank timely appealed to the Assessment Appeals Committee. In its appeal, the Bank incorporates by reference the arguments in its November 30, 2007 Request for Review. It also emphasizes its prior status as Well Capitalized, its history of parent company capital injections to maintain that status, the math error by which it fell to Adequately Capitalized, and the capital injections that returned the Bank to Well Capitalized on August 2, 2007. On these facts, the Bank contends that its increased assessment for the second quarter of 2007 is "unwarranted."

ANALYSIS

The Bank asks the Committee to elevate it from Risk Category II to Risk Category I for the assessment period beginning April 1, 2007.

Determination of Risk Categories is governed by 12 C.F.R § 327.9(a). Risk Category I institutions must meet a specified supervisory evaluation and a specified capital evaluation. 12 C.F.R § 327.9(a)(1). To be in Risk Category I, an institution must be assigned to Supervisory Group A, which is defined as a financially sound institution with only a few minor weaknesses. 12 C.F.R. § 327.9(c)(1). The Bank was correctly assigned to Supervisory Group A for the April 1, 2007 assessment period.

A Risk Category I institution must also be Well Capitalized. The issue presented turns on whether the Bank satisfied the regulatory standards required of Well Capitalized institutions.

To be Well Capitalized, an institution must satisfy three regulatory capital ratio standards: a Total risk-based capital ratio of 10 percent or greater; a Tier 1 risk-based capital ratio of 6.0 percent or greater; and a Tier 1 leverage capital ratio of 5.0 percent or greater. 12 C.F.R § 327.9(b)(1)(i). These capital evaluations are made "on the basis of data reported in the institution's Consolidated Reports of Condition and Income [(Call Report)] ... dated as of June 30 for the assessment period beginning the preceding April 1" 12 C.F.R § 327.9(b). The FDIC's regulations require a Well Capitalized institution to meet all three of these capital standards. AAC Case No. 2004-06 (January 13, 2005).

The Bank's June 30, 2007 Call Report indicated that it met the second and third of the Well Capitalized standards but fell short on the first: its Total risk-based ratio for the period in question was 9.72 percent, just under the 10 percent Well Capitalized threshold.

With a Total Risk-Based Capital Ratio of 9.72 percent (that is, lower than 10 percent but higher than 8 percent), the Bank was evaluated as Adequately Capitalized for the period in question. 12 C.F.R § 327.9(b)(2)(i). Adequately Capitalized institutions in

Supervisory Group A are assigned to Risk Category II (12 C.F.R. 327.9(a)(2)) and pay a higher deposit insurance assessment rate than Risk Category I institutions. 12 C.F.R. 327.10(b) (10 basis points versus 5 to 7 basis points). The Bank seeks reassignment to Risk Category I for the April 1, 2007 assessment period.

In considering past requests for similar relief, the Committee has looked to whether unique circumstances (generally, circumstances beyond the bank's control) prevented the bank from complying with the regulations or whether application of the capital regulations to the facts of the case would be inequitable. AAC Case No. 2004-06. The Bank bases its claim to relief on the grounds that it became Adequately Capitalized only as the result of a math error.

That the Bank's risk-based capital shortfall resulted from an inadvertent mistake in math does not affect the potential consequences either for the Bank or for the FDIC from the resultant decline in capital. As this Committee has previously ruled, risk-based capital is vitally important to the safety and soundness of the industry and to the FDIC; it provides a cushion against unexpected losses, reduces the risk of failure, and mitigates the FDIC's losses in the event of failure. The Committee has been - and remains - reluctant to sanction an exception to the Board's capital regulations for a bank's inadvertent failure to comply. AAC Case No. 2004-06.

To its credit, the Bank has a long history as a Well Capitalized institution and quickly took steps to raise its capital level on discovery of the shortfall. As the Committee has observed, that is one purpose of the regulation: to give banks an incentive to maintain strong capital levels. AAC Case No. 2004-06. We recognize that the Bank moved to restore its Well Capitalized status soon after the June 30, 2007 Call Report date, and did so on August 2, 2007, as verified by the OCC. But that does not excuse the Bank's failure to comply with the regulatory requirements for Well Capitalized institutions for the April 1, 2007 assessment period.

After considering all of the facts and arguments presented by the Bank in its appeal, the Committee finds that the circumstances presented are not unique nor is application of the capital evaluation regulation in this instance inequitable.

CONCLUSION

The Bank's capital evaluation for the April 1, 2007 assessment period was based on data reported in its June 30, 2007 Call Report. The Bank was correctly evaluated as Adequately Capitalized and assigned to Risk Category II for that period. While the Committee is sympathetic to the Bank's position and appreciates its efforts to return quickly to Well Capitalized status, no basis for granting relief from application of the

FDIC's regulations is presented here. Accordingly, for the reasons set forth in this decision, the Bank's appeal is denied.

By direction of the Assessment Appeals Committee, dated April 4, 2008.

Valerie J. Best
Assistant Executive Secretary